PROPOSED WELFARE EXEMPTION RULES
INTERESTED PARTIES THAT PROVIDED COMMENTS AFTER 1ST LIST POSTED

MARCH 11, 2005

Casa de la Paloma, March 2, 2005

Mercantile Capital Corporation, March 8, 2005

Non-Profit Housing Association of Northern California, The, March 4, 2005

WNC & Associates, Inc., March 11, 2005

Casa de
la Paloma

133 South Kenwood Street
Glendale, California 91205
(818) 243-0337

March 2, 2005

Mrs. Ladeena Ford
State Board of Equalization
Property and Special Taxes Department
P.O. Box 942879
Sacramento, CA 94279-0064

RE: March 16th Meeting Regarding Welfare Exemption Rules

Dear Mrs. Ford:

My name is Vardui Dzhuguryan; I am the administrator for Casa De La Paloma (CDLP), a 167-unit affordable housing community, located in Glendale, CA. CDLP is owned and operated by Southern California Presbyterian Homes, a not-for-profit corporation that has been in business for fifty years. CDLP has been in operations for 26-years and our resident population consists of seniors whose average age is 80 years and whose primary source of income is social security or supplemental security income. The need for affordable senior housing in Glendale far outweighs the supply of available units; there are 500 names on the CDLP waiting list, which is approximately 9 years long.

CDLP was developed using federally insured loans and state housing subsidies. The BOE's proposal to disqualify affordable housing projects financed with federally insured loans from eligibility for property tax exemptions will have a devastating impact on this property. Under our regulatory agreement, we cannot charge monthly rents greater than 30 percent of the resident's monthly income. Operating under a tight budget, there is little room to shift obligations around in the budget and begin paying property taxes. To do so, we would have to take money away from repairs and upkeep to the property, as well as services we have been able to offer residents to help keep them independent and in the community. If we were unable to absorb the additional costs, we would be in danger of violating our regulatory agreements and loan commitments.

If the BOE's proposal to disqualify projects financed by federally insured loans were the law in 1979, I don't think Casa De La Paloma would ever have been developed. Affordable housing projects are fragile, risky deals because the financing is so difficult to secure. Requiring such projects to pay property taxes would most likely render the deal financially untenable.

I believe that the type of subsidy used to finance affordable housing should not be the focus of whether an exemption applies or not. The test should be whether a property is required by contracts or regulatory agreements to keep rents restricted to an affordable level. I respectfully urge the BOE to maintain the current interpretations of who qualifies for exemption from property taxes.

Thank you for this opportunity to state my views.

Sincerely,

Vardui Dzhuguryan
Housing Administrator

cc: John Chiang, Fourth District County of Los Angeles
Claude Parrish, Vice-Chairman, Third District Counties of Imperial, Orange, Riverside, San Diego, a portion of Los Angeles, and a potion of San Bernardino

MERCANTILE CAPITAL CORPORATION

March 8, 2005

Dean R. Kinnee, Chief
Assessment Policy and Standards Division
California State Board of Equalization
Property and Special Taxes Department
450 N Street
Sacramento, CA 94279-0064

Re: Proposed Welfare Exemption Rules

Dear Mr. Kinnee:

Mercantile Capital Corporation and its affiliates have been lenders and investors in affordable multifamily housing properties in California for nearly 20 years. The purpose of this letter is to indicate our strong support for the BOE Staff Position on the welfare exemption rules.

Financing affordable housing in California is a difficult task. Costs are high, margins are thin, and loans and investments require long terms to pay out. In this environment, it is essential that regulatory requirements and tax policy for affordable housing be predictable, reliable and historically consistent. We believe that the BOE Staff positions accomplish this and should be followed.

Thank you for your consideration.

Sincerely,

James Keefe

James Keefe
President

JJK:jmc

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March 4, 2005

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Assessment Policy & Standards Division
State Board of Equalization

Dear Mr. Kinnee:

This letter represents the comments of the Non-Profit Housing Association of Northern California (NPH) related to the proposed welfare exemption rules outlined in the BOE's January 14th letter and again in its February 24th interested parties follow up memorandum.

NPH is a regional membership association founded in 1979 to advance affordable housing as the foundation for thriving individuals, families and neighborhoods. The membership of NPH, currently over 600 strong, draws together the main public, private, and non–profit partners active in the creation and support of affordable housing for low-income people in Northern California.

The following positions represent our current thinking about the proposed welfare exemption rules, as well as those of one of our sister organizations, the Southern California Association for Non-Profit Housing (SCANPH).

NPH members resoundingly support the welfare exemption as making the production and management of affordable housing possible. We support the Board's work to improve and strengthen the rules governing the exemption so that the standards are clear, and any abuse of the system is addressed with as much industry consensus as possible.

1. **Exemption qualification of tax credit properties.** We agree with the staff position. Properties that receive tax credits should be eligible for exemption for the duration of the longest regulatory agreement that meets BOE qualifications. It is the regulatory agreement that should be considered for determining eligibility, not any financing mechanisms.

2. **Exemption qualification of properties that have refinanced government loans.** Properties should remain eligible for exemption no matter whether loans are refinanced or not: the most restrictive regulatory agreement in effect for a property should remain the key determiner for the exemption.

3. **Exemption qualification of properties with federally-insured loans.** We support the staff position. Federally-insured loans with proper regulatory agreements should satisfy the "government financing" criteria under section

214, subd. (g)(1)(A). Financing should not determine whether an exemption is allowed; the regulatory agreement should.

4. **Amount of exemption allowed per property.** We agree with the staff position that the percentage of units specified in the most restrictive regulatory agreement should be eligible for exemption. In addition, NPH requests that the BOE clarify rules so that natural fluctuations are accommodated: (a) vacancies for restricted units are not to have the exemption revoked; (b) restricted units with over-income tenants do not lose the exemption unless the situation is uncorrected for two years; and (c) management units in projects governed by agreements are entitled to the exemption.

5. **Exemption qualification of property with multiple agreements.** We agree with the staff position. Where there are multiple regulatory agreements for a single project, the agreements should be combined to determine the percentage of units eligible for exemption.

6. **Exemption qualification of projects with section 8 tenant vouchers.** We agree with the staff position that units occupied by individuals with a section 8 voucher, in the absence of other sources of government financing, should not be qualified for the exemption. We do believe that project-based section 8 projects are good candidates for the exemption, however, since these projects are indeed tied to a regulatory agreement (Housing Assistance Payment contracts) keeping the units affordable to low-income people.

7. **Requirements for the nonprofit managing general partner.** We agree with the staff position that non-profit managing general partners must have management authority that it actually exercises, rather than merely functioning as a "shell." To best effectuate rules, NPH suggests the BOE approve the convening of a statewide industry-wide task force equally consisting of non-profit developers, for-profit developers, housing advocates, investors and other expert and interested parties to arrive at consensus regarding this issue. We suggest the task force be mandated to provide a range of possible rules for the Board's review, including a majority and minority report if needed, by a time certain. NPH and its members volunteer to be a part of such a taskforce.

8. **Qualifying rent levels.** We support the staff position. Projects which operate consistent with the regulatory agreement for the property regarding rent levels and/or that satisfy Health and Safety Code rent level requirements are eligible for exemption, and lower rents are not needed.

Thank you for considering our positions.

Sincerely,

Dianne J. Spaulding

Dianne J. Spaulding
Executive Director

WNC & ASSOCIATES, INC.

March 11, 2005

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Re: March 16, 2005 Meeting Proposed Rules: Welfare Exemption, Low Income Housing

Dear Ladies and Gentleman:

First, as always, thank you for the opportunity to present comments and concerns directed toward the proposed rule changes pertaining to the Welfare Exemptions described in Mr. Kinnee's January 14, 2005 letter to interested parties.

By way of background, our firm has invested in a very large number of low income housing [1] developments over the past thirty-three years. Accordingly, we are familiar with every aspect of the specialized financing for these apartment developments, as well as the ever- increasing need for more housing resources for the low to moderate income citizens of California. The property tax exemption for low income housing developers has become a key and irreplaceable component in the financing of affordable housing, due in part to increased land costs, city fees, construction costs, utility costs and insurance costs among many others.

[1] Low Income Housing as used in this letter means housing for individuals and families whose income fits within certain categories described in Health and Safety Code Sections 50053 & 50079.5. These California statutes take their lead from the federal Internal Revenue Code definitions of low income housing as contained in Section 42 of the IRC. The implementation of all housing programs in California focuses on "median income" numbers which are published by the federal Housing And Urban Development agency ("HUD") on an annual basis for each county in California.

In light of the overall California policy goals in mind, we are writing to you particularly regarding Proposed Rule(s) 140, 141, 142 and 143, as well as the "Issues 1-8" contained in Mr. Kinnee's January 14, 2005 letter.

The current "Low Income Housing Tax Credit" and the "Non-recourse Bond" programs under Section 42 of the Internal Revenue Code are two of the only major funding programs for low income housing construction in California. In addition, there are limited funds from the state and federal government (administered in California by the State Department of Housing and Community Development and ("HCD") and the California Housing Finance Agency, ("CalHFA"). There are also limited redevelopment agency ("RDA") funds available to assist the development of low income housing. The number and amount of subsidies has decreased over the last twenty years. A real need exists to maintain the Welfare Exemption for qualified developments.

Below is our response to the questions presented in Mr. Kinnee's letter:

ISSUE 1: Should Tax Credit Only Properties Have An Exemption After They No Longer Receive Tax Credits?

Of particular concern to us, is what we believe to be at least some of the Board staff's interpretation of Rev. & Tax § 214(g)(1)(A) & (B). That subsection states in pertinent part:

"(A) The acquisition, rehabilitation, development, or operation of the property, or any combination of these factors, **is financed with tax-exempt mortgage revenue bonds or general obligation bonds, or is financed by local, state, or federal loans or grants and the rents of the occupants who are lower income households do not exceed those prescribed by deed restrictions or regulatory agreements pursuant to the terms of the financing or financial assistance**.

(B) The owner of the property is **eligible for and receives low-income housing tax credits pursuant to Section 42 of the Internal Revenue Code of 1986, as added by Public Law 99-514.**"

It has come to our attention that there is some debate at the Board or with staff regarding the length of time an otherwise qualifying project and developer/ owner maintains his/ her or its financing qualifications under Section 214(g). With this understanding in mind, we focus on the particular words of the statutes we think are in dispute. In particular, we believe the meaning of the word "receive" in subsection (B) above vis a vis the "receipt" of low income housing tax credits, which is one of the alternative forms of financing qualifying an ownership entity under Revenue and Taxation Code Section 214(g), is simply that the project "receive" the credits at some point in time, (in the same or similar fashion it would "receive" the proceeds from a loan closing or a bond closing). [2]

Our understanding of "receipt" in this statutory context is that the limited partnership "receives" a reservation letter from the California Tax Credit Allocation Committee (which has been previously approved by the Board staff as adequate under 214 (g)(A)(i) and (ii) as the equivalent of a recorded deed restriction or a verifiable agreement with a public agency) and then later "receives" an actual allocation of low income housing tax credits.

[2] This meaning of the word "receipt" is consistent with *Webster's New World Dictionary College Ed.* (1991), at pg. 1120 and *Ballentine's Law Dictionary* (1969).

We do not believe a fair reading of this subsection would imply the words "continually receives throughout the period the tax exemption is claimed" or language to that effect. The statutory language is un-ambiguous in that it refers to simply "receipt" and not "annual receipt" or "continual receipt" for some extended period of time. Therefore, the fact that the limited partnership / developer has actually "received" the reservation letter, then later received the tax credits from the CTCAC, should be sufficient to comply with this ordinary and unambiguous sentence of Subsection B quoted above.

In fact, if this use of the word "receive" were given any other interpretation, it could lead to absurd results. For example, if the limited partnership "received" its permanent loan on a particular day, say the date of the real estate loan closing; that would be the only day it "received" the funds, although the lender would place (low income) restrictions on the borrower for 30 or more years. We can't imagine that SBOE would take the position that the property tax exemption based on other financing sources pursuant to Rev. & Tax § 214(g)(1)(A) would exist only on the date the loan closed and perhaps this situation is made more clear by the extension of the paragraph in subsection (A) which adds the fact that the rents charged to the tenants will not exceed those described in the deed restrictions or regulatory agreements (which obviously extend for 30 to 55 years even though technically speaking the "financing" may have occurred in one 24 hour period.

Statutory interpretation requires ascertainment of the intent of the Legislature under familiar and established principles.

> "[i]f the language of the statute is not ambiguous, the plain meaning controls and resort to extrinsic sources to determine the Legislature's intent is unnecessary." (Ibid.) When the statutory language is unambiguous, " 'we presume the Legislature meant what it said and the plain meaning of the statute governs.' " (*Diamond Multimedia Systems, Inc. v. Superior Court* (1999) 19 Cal.4th 1036, 1047.)

ISSUE # 2: Should Low Income Developments Still Receive Property Tax Exemption After Their Financing Is Paid Off ?

For the sake of brevity, using the same analysis above, the key to Issue #2 is whether or not the apartment project is restricted by a regulatory agreement. For example, as mentioned above, in order to achieve maximum "points" in the competition for the 9% tax credits and 4% credits associated with non-recourse bond funding, the developers typically agree to a 55 year regulatory period. However, the funding structure, which is usually a combination of a "construction" loan, which last perhaps 2 years while the project is being completed, then a "permanent" loan which extends normally for a term of 30 years. Often there are other (e.g. City RDA or HOME) funding sources added to the total "permanent" financing. However, typically, all the "permanent financing" is due on or before the end of thirty (30) years, but the tax credit regulatory agreement normally extends to fifty –five (55) years. That is the **low-income rent structure** which is the key to this property tax exemption, is mandated (and agreed upon) for at least fifty-five years.

The problem has not arisen yet, as the tax credit program and the tax exemption under Section 214(g) itself has have existed approximately the same length of time, which is less than 20 years, but our position is that, since the intent of the Legislature in 1988 [3] was the creation of a

[3] The Welfare Exemptions as a whole were first adopted as a California Constitutional amendment November 7, 1944. [Assessor's Handbook, Section 267, Pg. 1, fn. 3]

property tax exemption for apartment projects in which the owners / developers with the proper internal structure agreed to a binding deed restriction and/ or regulatory agreement restricting rent levels to those prescribed in Health & Safety Code §§ 50053 & 50079.5, the property tax exemption should not automatically or at least necessarily end even after 55 years under the original regulatory agreement, so long as the owner of the property still has the appropriate internal structure to support application for the exemption and agrees to another recorded regulatory agreement restricting the rents charged to the tenants for an additional period of time. [See for e.g. the requirements for deed restriction or enforceable agreement contained in the Assessor's Handbook, Section 267, pg. 67]

The focus of this exemption has always been to facilitate the construction and maintenance of decent, safe and sanitary apartment units affordable to households earning at or near 1/2 the median income as established by HUD for each county in California. [4] The situation of lower income individuals desperately needing adequate housing is unlikely to change in the near future, therefore the exemption should continue as long as the criteria set forth in Section 214(g) are met by a given limited partnership and its project. ***Similarly, in the event said exemptions were denied to projects otherwise complying with Section 214(g) and government agency rent restrictions imposed for 55 years in most cases, many, if not all, projects would no longer be financially feasible (due to the imposition of property taxes and the prohibition against raising rents) relative to meeting debt service obligations to the lender(s) and would ultimately suffer foreclosure. [5] This would in turn result in the formerly "affordable" units being removed from the low income housing stock and converted to market rate housing. We respectfully submit to you that this was not the legislative intent behind Section 214(g).***

ISSUE # 3: Do Federally Insured or Guaranteed Loans Constitute Government Financing Under Rev. & Tax Code § 214(g)(1)(A)?

The words of the statute are the following:

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[4] Most regulatory agreements of tax credit projects mandate rent levels based on 50% to 60% of county median income, or less.

[5] The investors and lenders involved in all projects with the Section 214(g) property tax exemption have underwritten their investment and / or loan pro-forma as the case may be in reliance upon the tax exemption. Each investment firm and lender has in turn entered into various agreements with its own individual investors, board of directors or other firms who have relied upon its underwriting. Any significant change to the 214(g) exemption interpretation or process should take into account the obvious correlation between the certification by the managing general partner that the tax exemption is necessary to maintain the affordability of the rents and thus, the entire project's economic viability and the fact that rule changes by SBOE "after-the-fact" such as shortening the period the exemption is available based on the "received" argument mentioned in Issue Number 1 above, would have catastrophic effects on not only the low income developments themselves, but many related businesses which relied upon the project's continued exemption.

> **"(A) The acquisition, rehabilitation, development, or operation of the property, or any combination of these factors,** is financed with tax-exempt mortgage revenue bonds or general obligation bonds, or is financed by local, state, or federal loans or grants...."

Therefore, according to the language of the statute, one of the alternatives to meet the terms of Section 214(g) is financing by (any)"... local, state, or federal loans or grants...."

Issue # 3 is a bit vague, as it posits the question whether a federally insured or guaranteed loan qualifies as "government financing", whereas Section 1(A) does not mention the term "government financing" nor does it mention "federally insured or guaranteed". It simply states "local, state or federal loans or grants..."

ISSUE # 4: Should The Tax Exemption Be Limited To Certain Percentages As Expressed In A Particular Regulatory Agreement?

The short answer to this question is "no". The reason is that there are various regulatory agreements from different funding sources and the reasons each regulatory agreement states for mandating that a particular number of apartment units be restricted to certain rent levels differ, but usually do not control the total number of low-income units in the apartment project. For example, as mentioned in the preamble paragraph above, HOME funds are from a federal program. They are administered in the State of California by the State Department of Housing And Community Development, ("HCD"). HCD's regulatory agreements for home funds typically mandate that less than 49% of the units are restricted to low income housing *to receive HCD's HOME funding.* The regulatory agreement from HCD is structured this way in part because of "Article XXXIV" of the California Constitution, which arguably mandates a local election in the event more than 49% of the apartment units are restricted *by the HCD regulatory agreement.* [see *California Housing Finance Agency v Elliot*, 17 Cal. 3d 575 (1976) and also see Public Housing Election Implementation Law, codified at Health and Safety Code §§ 37000-37002 (the "Act"). However, in projects with HCD/ HOME funding, most are also regulated by a "tax credit" regulatory agreement from the California Tax Credit Allocation Committee and in that agreement, the developer agrees to restrict 100% of the units are affordable within the meaning of Health & Safety Code Sections 50053 and 50079.5.

Another point on this issue is that the current practice of SBOE and the county assessors is to require specific qualifying tenant information for each apartment unit which is claimed to be exempt. Therefore, it would seem there is already a test in place to insure that the applicant is not claiming more units as exempt than actually qualify.

In summary, the answer to this issue is that the percentage of exemption should remain as the percentage of qualifying tenants which are verified by the applicant in either the "first filing" or the "annual filing" for tax exemption, not a number taken from a regulatory agreement. Secondly, each regulatory agreement should be considered together when asking the question how many units are restricted. That is, if one regulatory agreement restricts 49% of the units, but another restricts 100%, then the higher number should be used in this inquiry.

ISSUE # 5: Should Multiple Regulatory Agreements Be Combined?

Part of this answer has been given in Number 4 above. There are concrete reasons that different regulatory agreements recorded against the title to the same apartment development have different percentages of mandatory restrictions on numbers of units in the project. [see #4 ante re: Article XXXIV issues] Therefore, if there are two or three regulatory agreements, each mandating a different number of units to be restricted to low income qualified tenants, the highest number of restricted units in any one agreement or the aggregate number in all the agreements as the case may be, should be used.

ISSUE # 6: Do HUD Vouchers Or Project Based Assistance Qualify As "Government Financing"?

Again, Section 214 (g) does not mention the term "government financing". Section 214(g) refers only to "... local, state, or federal loans or grants...." As recognized by this Issue # 6 statement , Section 8 assistance comes in two basic varieties, (1) project based and (2) voucher. The distinguishing characteristic of a voucher is that it is "personal" to the tenant. In other words, once the local housing authority issues a voucher to a tenant, she can use the voucher at apartment project "A" or "B". Since this "portability" feature means that assuming arguendo that the voucher is some type of "government financing", it is not mandated that it be tied to any particular apartment development. Project based Section 8 on the other hand is specific to the project. Project based Section 8 is routinely considered in the underwriting by "syndicators" (purchasers of the low income housing tax credits) and lenders, when calculating the debt service and income of a particular project. In other words, the project based Section 8 is a government "benefit" paid to a given apartment project and it is accompanied by a restrictive agreement mandating that the apartment project charge rents within a certain structure which comports with the rents described in Health and Safety Code Sections 50053 and 50079.5 as low-to-moderate income rents.

In summary, our opinion is that the vouchers are not "government financing" to any particular apartment project, whereas the "project based" Section 8 most certainly is.

ISSUE # 7: Should the Management Duties Of the Managing General Partner Be Strengthened?

The short answer to this question is again, "no". The SBOE insisted that there be adequate language in the limited partnership agreement to describe the duties of the managing general partner and to illustrate that the duties were regular, substantial and continuous, (using the terminology of the IRS). Low income housing developers and nonprofits, which are the MGP's of qualified limited partnerships, *want to comply* with SBOE's rules and regulations and the SBOE needed to make it clear what exact type of language was sufficient.

In the summer of 1999, SBOE gave the low income housing development community specific language in the form of three "examples" of appropriate managing general partner language for the partnership agreements. On December 19, 2002, SBOE approved two new forms, the Supplemental Affidavit, (BOE-267-L-1) and (BOE-267-L-2). The intent of these forms was to "streamline" the filing and review process of exemption claims for lower income housing." These forms were developed after SBOE staff found it had been inundated with partnership agreements to review, as it had established as criteria for granting the property tax exemptions

that there had to be a "dual review" of each application and each partnership agreement (one review by the county assessor and another by SBOE staff).

This 2002 change in procedure by the SBOE staff was in fact a "streamlining" of the process. Board staff didn't have to review all of the partnership agreements any longer, and the Managing General Partner of each partnership certified in writing to the SBOE and the county assessor that the partnership agreement met the tests set forth in the "laundry list" of possible duties listed on the BOE-267-L-1 and BOE-267-L-2 forms.

Later in November of 2002 SBOE introduced the BOE –277 form (the Organizational clearance Certificate form) and still a little later, its companion form, the BOE-277-L-1 (Supplemental Clearance Certificate) the latter of which further clarifies the role of the managing general partner and asks the managing general partner to again certify that the operable limited partnership agreement contains the appropriate language which adequately outlines the duties and responsibilities of the managing general partner per SBOE's guidelines.

The long and short of this issue is that the SBOE over the past ten (10) years has made it abundantly clear what its desires are as far as duties of the managing general partner and the Board now requires the managing general partner to certify on two separate forms that it has met the requirements set forth by SBOE. [see, eg. SBOE letter of May 7, 2004 to Assessors and Interested Parties, Attachment C, pg. 9, footnote 19] For example, on the BOE-277-L-1 (Supplemental Clearance Certificate) form, the managing general partner is asked to swear that the nonprofit has "control over the business, assets and affairs of the partnership" [BOE-277-L-1, @ ¶ 11 (A)(1) and that the managing nonprofit partner satisfies at least two of the ***nineteen separate duties*** enumerated by SBOE in subparagraph 11 (A)(2). No further consideration of "duties" is needed.

ISSUE # 8: Does Rev. & Tax. Code Section 214 (g)(2)(B) Require Lower Rents Than Either The Codes or the Regulatory Agreement ?

The answer is "no", Section 214(g) does not require lower rents than those already established by HUD through its Section 8 program and the publishing of the "median income figures" for each California county mentioned above.

Section 50079.5 of the Health and Safety Code reads as follows:

> HSC §50079.5. (a) "Lower income households" means persons and families whose income does not exceed the qualifying limits for lower income families as established and amended from time to time pursuant to Section 8 of the United States Housing Act of 1937. The limits shall be published by the department in the California Code of Regulations as soon as possible after adoption by the Secretary of Housing and Urban Development. In the event the federal standards are discontinued, the department shall, by regulation, establish income limits for lower income households for all geographic areas of the state at 80 percent of area median income, adjusted for family size and revised annually.

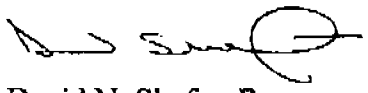
The HUD median income numbers are published by HUD on a county-by –county basis for the State of California as well as other states and are the same benchmark used by the California Tax Credit Allocation Committee and the California Debt Limit Allocation Committee as well

as all other California low income housing organizations to compute the appropriate county-by-county rent structures for given family sizes.

Thank you so much for taking the time to read and consider this letter and for your assistance and participation in this important area of the law for low income households who are the primary beneficiaries of Section 214(g).

Sincerely,

WNC & Associates, Inc.



David N. Shafer, Esq.
Executive Vice President

DNS/ml